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**SUMMATIVE (FORMAL) ASSESSMENT: MODULE 3A**

**THE INSOLVENCY SYSTEM OF THE UNITED STATES**

This is the **summative (formal) assessment** for **Module 3A** of this course and is compulsory for all candidates who **selected this module as one of their compulsory modules from Module 3**. Please read instruction 6.1 on the next page very carefully.

If you selected this module as **one of your elective modules**, please read instruction 6.2 on the next page very carefully.

**The mark awarded for this assessment will determine your final mark for Module 3A**. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

**INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT**

**Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.**

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.

2. All assessments must be submitted electronically in MS Word format, using a standard A4 size page and a 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way**. **DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.

3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).

4. You must save this document using the following format: **[studentID.assessment3A]**. An example would be something along the following lines: 202223-336.assessment3A. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “student number” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked**.

5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words**.

6.1If you selected Module 3A as one of your **compulsory modules** (see the e-mail that was sent to you when your place on the course was confirmed), the final time and date for the submission of this assessment is **23:00 (11 pm) GMT on 1 March 2023**. The assessment submission portal will close at 23:00 (11 pm) GMT on 1 March 2023. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.

6.2 If you selected Module 3A as one of your **elective modules** (see the e-mail that was sent to you when your place on the course was confirmed), you have a **choice** as to when you may submit this assessment. You may either submit the assessment by **23:00 (11 pm) GMT on 1 March 2023** or by **23:00 (11 pm) BST (GMT +1) on 31 July 2023**. If you elect to submit by 1 March 2023, you **may not** submit the assessment again by 31 July 2023 (for example, in order to achieve a higher mark).

7. Prior to being populated with your answers, this assessment consists of **9 pages**.

**ANSWER ALL THE QUESTIONS**

**QUESTION 1 (multiple-choice questions) [10 marks in total]**

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and mark your selection on the answer sheet by highlighting the relevant paragraph **in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

**Question 1.1**

Which of the following entities **does not** satisfy the minimum presence requirement to be a debtor under any chapter of the Bankruptcy Code?

1. A foreign domiciled company that pays a US attorney a retainer.
2. A company with several US bank accounts, but no physical presence in the United States.
3. A company with US patents, but no physical presence in the United States.
4. All of the above satisfy the minimum requirement for presence in the United States.
5. None of the above satisfy the minimum requirement for presence in the United States.

**Question 1.2**

ABC Corp is an industrial manufacturing company that is filing for bankruptcy. Which of the following **could not** be considered a party in interest?

(a) A neighboring landowner to ABC Corp’s manufacturing plant.

(b) An environmental advocacy group that opposes ABC Corp’s operations.

(c) The landlord of ABC Corp’s corporate office.

(d) People who live several miles downstream from ABC Corp’s manufacturing plant and have been exposed to the plant’s toxic waste.

(e) The US Internal Revenue Service.

**Question 1.3**

Which of the following contracts to which ABC Corp is a party is executory and may be assigned without counterparty consent?

1. A lease on a manufacturing plant that contains a provision that requires landlord approval of any assignment.
2. An employment contact between ABC Corp and a former employee, requiring the company to provide health insurance through the end of the current year.
3. A 10-year software licensing agreement with XYZ Corp that is three years into performance.
4. A lease on office space that ended the prior year, but for which ABC Corp still owes past rent.
5. None of the above are executory and may be assigned without counterparty consent.

**Question 1.4**

Which of the following conditions **must** be true about a reorganization plan for a court to confirm it under Chapter 11 proceedings?

1. Have a possibility of success, even if it relies on speculative or improbable events to be capable of execution.
2. The plan is not likely to be followed by liquidation.
3. All impaired classes must accept the plan.
4. All of the above.
5. None of the above.

**Question 1.5**

Which of the following about cramdowns, is **false**?

1. The plan of reorganization must be fair and equitable to all impaired classes.
2. Differential treatment of different classes is permitted if there is a reasonable, good faith basis for doing so and such treatment is required for the plan of reorganization to be successful.
3. Class definition is often a battleground when a debtor tries to cramdown classes.
4. Dissenting creditors are permitted to challenge the classification of a creditor supporting the cramdown.
5. If one insider creditor approves of the plan of reorganization, all other impaired classes may be crammed down.

**Question 1.6**

Which of the following about 363 sales is **false**?

1. A good faith purchaser at a 363 sale may retain the property notwithstanding a subsequent reversal of court approval for the sale on appeal.
2. The debtor in possession must establish that the transaction is in the best interests of the estate as a whole.
3. In chapter 15 proceedings, a foreign court’s approval alone suffices for a 363 sale.
4. Debtors must carry out a robust marketing process for the sale.
5. A creditor’s lien on assets sold in a 363 sale attaches to the proceeds of the sale.

**Question 1.7**

Which of the following is true of both an actual fraudulent conveyance and a constructive fraudulent conveyance?

1. The debtor must have had an actual intent to hinder, delay, or defraud any entity to which the debtor was or became indebted.
2. Both require at least circumstantial evidence of the fraudulent intent.
3. The debtor must have been insolvent at the time of transaction.
4. In addition to provisions in the Bankruptcy Code, the debtor or the trustee may invoke applicable state or foreign fraudulent conveyance laws.
5. All of the above are true.

**Question 1.8**

**When** does an automatic stay come into effect?

1. Immediately on the filing of any plenary petition.
2. On the filing of a voluntary petition but not on the filing of an involuntary petition.
3. Once the court reviews the petition and grants the stay.
4. Once the petitioner announces their intention to file for bankruptcy publicly.
5. Once a plan of reorganization is confirmed.

**Question 1.9**

Which of the following regarding substantive consolidation is **true**?

1. It respects the boundaries of corporate separateness.
2. It is the treatment of two or more creditors as a single creditor to simplify the claims process.
3. If a creditor can show it extended credit on the basis of corporate separateness, it has a valid objection to substantive consolidation.
4. Substantive consolidation is commonly used to resolve bankruptcies of corporate groups.
5. Authority for substantive consolidation comes from the Bankruptcy Code.

**Question 1.10**

Which of the following are relevant factors in determining a debtor’s center of main interests (COMI) in the recognition stage of a Chapter 15 bankruptcy case?

1. The location of the headquarters.
2. The location of primary assets.
3. The location of the majority of the affected creditors in the request for relief.
4. The jurisdiction whose law will apply to most disputes.
5. All of the above.

**QUESTION 2 (direct questions) [10 marks]**

**Question 2.1 (1 mark)**

What is setoff and why is it not permitted in many circumstances?

According to HALL, “[s]etoff permits a creditor holding a claim against the debtor and simultaneously owing money to the debtor to net out the two (or more) obligations”.[[1]](#footnote-1) A setoff is not permitted in many circumstances because they may give unequal treatment of creditors in similar situations, by improving a creditor's position compared to others.

**Question 2.2 [2 marks]**

What rules should you review when preparing a filing for a bankruptcy court?

The relevant rules for a bankruptcy case are the Federal Rules of Bankruptcy Procedure (the Bankruptcy Rules), the Federal Rules of Civil Procedure and the local rules of the bankruptcy court. It is also important to review the judge's personal practices.[[2]](#footnote-2)

**Question 2.3 [2 marks]**

What does the absolute priority rule require and when can it be deviated from?

According to HALL, “[t]he absolute priority rule requires that payment in full must be made to each category of claims before the next category receives anything”.[[3]](#footnote-3) The absolute priority rule can be deviated with the consent of affected creditors, only in case of Chapter 11.[[4]](#footnote-4)

**Question 2.4 [2 marks]**

What is a “priming lien” and what requirements must be met for such a lien to be granted to secure DIP financing?

HALL defines that a “priming lien” “is senior or equal to a pre-petition lien on estate property to secure post-petition financing”.[[5]](#footnote-5) The court may grant a priming lien if the debtor cannot obtain a DIP on any other terms. Moreover, HALL indicates that "[t]he debtor also must demonstrate that the interest of the secured creditor being primed is adequately protected".[[6]](#footnote-6)

**Question 2.5 [3 marks]**

What is a preference? What are the elements of a preference claim that need to be proved? Is a showing of fault, by either the debtor or creditor, required?

According to HALL, “preference is a transfer of the debtor’s property made in a suspect period before the petition date that must be returned to the estate if it exceeds the amount the recipient would have received in a chapter 7 liquidation had the transfer not been made”.[[7]](#footnote-7) There are six elements of a preference claim that need to be proven: (a) a transfer of an interest of the debtor in property; (b) that the transfer was mad to or for the benefit of a creditor; (c) that the transfer was made for or on account of an antecedent debt owed by the debtor; (d) that the transfer made while the debtor was insolvent, considering that the debtor is presumed to have been insolvent on and during the 90 days prior to the petition date for purposes of determining preference claims; (e) that the transfer was made during the suspect period, that is 90 days prior to the petition; and (f) that enables the creditor to receive more than it would have in a chapter 7 liquidation.[[8]](#footnote-8) It is not required to show of fault by either the debtor or creditor.[[9]](#footnote-9)

**QUESTION 3 (essay-type questions) [15 marks in total]**

**Question 3.1 [3 marks]**

Describe the circumstances in which a bankruptcy court may enter a final order, who reviews appeals from bankruptcy court orders and how are non-final orders reviewed?

According to HALL, in response to the US Supreme Court, new jurisdictions provisions “creates a distinction between “core” and “non-core” matters, and permits bankruptcy judges to hear and determine only core proceedings”.[[10]](#footnote-10) The § 157(b)(2) of 28 USC provides a non-exhaustive list of core proceedings:

“(2) Core proceedings include, but are not limited to—

(A) matters concerning the administration of the estate;

(B) allowance or disallowance of claims against the estate or exemptions from property of the estate, and estimation of claims or interests for the purposes of confirming a plan under chapter 11, 12, or 13 of title 11 but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims against the estate for purposes of distribution in a case under title 11;

(C) counterclaims by the estate against persons filing claims against the estate;

(D) orders in respect to obtaining credit;

(E) orders to turn over property of the estate;

(F) proceedings to determine, avoid, or recover preferences;

(G) motions to terminate, annul, or modify the automatic stay;

(H) proceedings to determine, avoid, or recover fraudulent conveyances;

(I) determinations as to the dischargeability of particular debts;

(J) objections to discharges;

(K) determinations of the validity, extent, or priority of liens;

(L) confirmations of plans;

(M) orders approving the use or lease of property, including the use of cash collateral;

(N) orders approving the sale of property other than property resulting from claims brought by the estate against persons who have not filed claims against the estate;

(O) other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship, except personal injury tort or wrongful death claims; and

(P) recognition of foreign proceedings and other matters under chapter 15 of title 11”.[[11]](#footnote-11)

A US bankruptcy proceeding can have final and interlocutory orders. HALL defines that “[f]inal orders are those that dispose of all issues, leaving nothing further to be decided, whereas interlocutory orders resolve only some issues or claims. Final orders may be appealed as of right, whereas interlocutory orders may be appealed only with leave of the appellate court”.[[12]](#footnote-12) As an exception "orders extending the period of exclusivity to propose a plan are appealable as of right".[[13]](#footnote-13) Furthermore, in Bullard v Blue Hills Bank, 135 S Ct 1686 (2015) “the US Supreme Court has held that a bankruptcy order resolving a discrete dispute is a final order for appeals purposes”.[[14]](#footnote-14)

On appeal, such orders may be directed to the district court, a Bankruptcy Appellate Panel (BAP) or directly to the court of appeals. HALL describes the criteria for such referral:

“In general, appeals from bankruptcy court decisions are heard by the district court for the district in which they sit. In certain circuits, however, bankruptcy appeals are heard by a Bankruptcy Appellate Panel (BAP), convened from the judges of the bankruptcy courts within the circuit. In those circuits, a party has the option to request that the appeal be heard by the district court instead. From the district court or BAP, there is a further appeal of right (assuming the initial order was one from which an appeal of right was available) to the circuit court of appeals. In rare circumstances, an appeal from a bankruptcy court may go directly to the court of appeals, where the bankruptcy court or district court certifies that either that (i) the appeal raises a question of law as to which there is no controlling decision of the circuit or the US Supreme Court, or requires resolving conflicting controlling decisions, or (ii) immediate appeal may materially advance the progress of the case. The court of appeals has discretion whether to accept a case so certified”.[[15]](#footnote-15)

The author concludes that in case of a final order in a core proceeding, “the district court or BAP reviews conclusions of law de novo and reviews findings of fact for abuse of discretion”.[[16]](#footnote-16)

Regarding non-core proceedings, HALL points out that

“As to non-core proceedings, the bankruptcy court may hear the non-core proceedings if they are sufficiently related to a bankruptcy proceeding,31 but cannot make a final determination; instead, it submits proposed findings of fact and conclusions of law to the district court, to which interested parties may object, for the district court’s final decision”.[[17]](#footnote-17)

In this scenario, the author concludes that

“If the ruling was in a noncore proceeding or the bankruptcy court otherwise did not have authority to enter a final order, the district court or BAP reviews de novo all findings of fact and conclusions of law to which a party has objected. The order of a district court or BAP is reviewed by a circuit court of appeal de novo as to conclusions of law and for abuse of discretion for findings of fact”.[[18]](#footnote-18)

Therefore, the bankruptcy court can give final orders in cases of core proceedings, pointed out non-exhaustively by § 157(b)(2) of 28 USC. Bankruptcy court appeals may be reviewed by the district court, a BAP or directly to the court of appeals, depending on the case. In addition, the difference in the review of the ruling in anon-core proceeding is that there is a broader analysis of the facts by the district court or BAP.

**Question 3.2 [3 marks]**

What provisions of the Bankruptcy Code automatically apply to the debtor’s property within the territorial jurisdiction of the United States upon recognition of a foreign main proceeding? What relief may be granted on a discretionary basis for either foreign main or non-main proceedings?

Chapter 15 of the 11 USC does not reproduce the UNCITRAL Model Law on Cross-Border Insolvency (Model Law) definition of “foreign representative”. According to Section 2(d) of the Model Law, foreign representative “means a person or body, including one appointed on an interim basis, authorized in a foreign proceeding to administer the reorganization or the liquidation of the debtor’s assets or affairs or to act as a representative of the foreign proceeding”.

The foreign representative can file a petition under Chapter 15 of the 11 USC for recognition of a foreign proceeding. In this moment, the foreign representative can request relief where it is urgently needed to protect the assets of the debtor or the interests of the creditors. The court may grant relief in terms of § 1519(a) of the USC. The relief of a provisional nature, including (a) “staying execution against the debtor’s assets”;[[19]](#footnote-19) (b) “entrusting the administration or realization of all or part of the debtor’s assets located in the United States to the foreign representative or another person authorized by the court”;[[20]](#footnote-20) (c) “suspending the right to transfer, encumber or otherwise dispose of any assets of the debtor”;[[21]](#footnote-21) (d) “providing for the examination of witnesses, the taking of evidence or the delivery of information concerning the debtor’s assets, affairs, rights, obligations or liabilities”;[[22]](#footnote-22) and (e) “granting any additional relief that may be available to a trustee, except for relief available under sections 522, 544, 545, 547, 548, 550, and 724(a)”.[[23]](#footnote-23) This applies both in the case of a petition for recognition of a foreign main proceeding and a foreign non-main proceeding.

A foreign main proceeding is defined as “a foreign proceeding pending in the country where the debtor has the center of its main interests”.[[24]](#footnote-24) When a U.S. court recognizes a primary foreign proceeding, the following provisions of the Bankruptcy Code are automatically applied: (a) “automatic stay”;[[25]](#footnote-25) (b) “operation of the debtor’s business in the ordinary course by the foreign representative”;[[26]](#footnote-26) (c) “sale, transfer or use of property outside the ordinary course”;[[27]](#footnote-27) and (d) “avoidance of post-petition transfers and post-petition perfection of security interests”.[[28]](#footnote-28)

The U.S. court may grant additional relief on a discretionary basis for a foreign main proceeding. In this case, § 1521(a) of the 11 USC provides the following provisions: (a) “authorization of discovery regarding the debtor’s assets and affairs”;[[29]](#footnote-29) (b) “entrusting administration of the debtor’s US assets to the foreign representative or other person”;[[30]](#footnote-30) (c) “extension of provisional relief”;[[31]](#footnote-31) and (d) “any other relief ‘necessary to effectuate the purposes of [chapter 15] and to protect the assets of the debtor or the interests of creditors’”.[[32]](#footnote-32)

In the case of recognition of a foreign non-main proceeding by the US court, all the above relief may be granted on a discretionary basis be granted at the discretion.[[33]](#footnote-33)

Therefore, Chapter 15 adopted the Model Law in which it preserves the difference between the relief granted in case of recognition of foreign main proceeding and a foreign non-main proceeding. In this sense, the foreign main proceeding has the advantage of some automatic relief provisions, while the foreign non-main proceeding depends on the discretion of the US court.

**Question 3.3 [4 marks]**

What duties do directors owe to a Delaware corporation in the ordinary course of business? To whom are these duties owed when the corporation is potentially or actually insolvent? What rule protects directors from liability for errors of judgment?

In the ordinary course of business, “[d]irectors owe a fiduciary duty of loyalty to the corporation’s best interest and a duty of care in educated decision-making”.[[34]](#footnote-34) The business judgment rule protects directors from liability for errors of judgments. According to HALL:

“Under the business judgment rule, the board of directors is presumed to have acted in good faith on the basis of reasonable information. This presumption can be rebutted only by showing that a majority of the board in fact were not reasonably informed, did not honestly believe that their decision was in the corporation’s best interest, or were not acting in good faith. Unless the presumption is rebutted, the directors will not be liable in the absence of a showing of gross negligence”.[[35]](#footnote-35)

The fact that the corporation is potentially or actually insolvent does not affect the director's duties. HALL indicates that “[d]irectors’ duties are owed to the corporation and its shareholders, not to creditors”.[[36]](#footnote-36) The Delaware Supreme Court held in North Am Catholic Educational Programming Foundation, Inc v Gheewalla, 930 A.2d 92, 103 (Del 2007) that directors of an insolvent corporation have no duties to the corporation's creditors.[[37]](#footnote-37)

**Question 3.4 [5 marks]**

List and describe the requirements that a creditor’s claim must fulfill in order to qualify as a petitioning creditor in an involuntary proceeding.

A creditor or group of creditors may commence involuntary reorganization (chapter 11) or liquidation (chapter 7) proceedings against a particular debtor.[[38]](#footnote-38) The number of creditors needed to initiate an involuntary proceeding depends on the number of non-contingent and non-insider creditors the debtor has. If the debtor has less than twelve creditors under these conditions, a single creditor may commence an involuntary procedure. Otherwise, at least three creditors are needed to do so.[[39]](#footnote-39)

The requirements that a creditor’s claim must fulfill in order to qualify as a petitioning creditor in an involuntary proceeding, according to HALL, are: (a) “Non-contingent”;[[40]](#footnote-40) (b) “Not the subject of bona fide dispute as to liability or amount”;[[41]](#footnote-41) and (c) “Unsecured or undersecured, separately or in the aggregate with all other petitioning creditors’ claims, in the amount of at least USD 16,750 (this amount is periodically increased due to inflation)”.[[42]](#footnote-42)

For the first requirement to be met, the creditor's claim must be non-contingent. A non-contingent claim is one that does not depend on the occurrence of a future event to be enforceable.[[43]](#footnote-43) Even so. HALL points out that “[a] debt that is unmatured (because the payment is due in the future) is not contingent if all requirements for liability, other than the passage of time, have occurred".[[44]](#footnote-44)

As for the second requirement, it is observed that the responsibility or value of the claim cannot be the subject of bona fide dispute. According to HALL, “[a] bona fide dispute exists if there is an objectively reasonable basis for a dispute as a matter of fact or law; the debtor’s subjective belief that the debt is not owed or the amount claimed is incorrect is not sufficient”.[[45]](#footnote-45) In other words, the debtor cannot have justifiable reasons to challenge a claim. Even if the dispute involves only part of the claim, the creditor cannot use the undisputed portion to initiate involuntary proceedings. However, other undisputed creditor claims are not disqualified because of disputes of other claims held by the same creditor.[[46]](#footnote-46)

The third and final requirement involves the need for creditors, separately or jointly, to demonstrate that they have claims in a minimum amount, which is updated periodically. HALL indicates that

“Unlike the voluntary petition, which requires no allegation of insolvency, the involuntary petition form requires the petitioning creditors to allege either that the debtor is generally not paying its debts as they become due, unless they are the subject of a bona fide dispute as to liability or amount or that, ‘within 120 days before the filing of this petition, a custodian, other than a trustee, receiver, or an agent appointed or authorized to take charge of less than substantially all of the property of the debtor for the purpose of enforcing a lien against such property, was appointed or took possession’”.[[47]](#footnote-47)

Therefore, to qualify as a petitioning creditor in an involuntary proceeding, their claims must be non-contingent, their claim cannot be the subject of bona fide dispute as to liability or amount, and they must demonstrate that the debtor is insolvent, in this case, demonstrating that, without justification, it failed to pay claims totalling a minimum amount that is updated periodically.

**QUESTION 4 (fact-based application-type question) [15 marks in total]**

**Question 4.1 [5 marks]**

Speculation Inc is engaged in day-trading stocks from leased office space with two employees. It funds its trading through a margin loan from its broker, where the shares it purchases are held as collateral. For a while, Speculation Inc was very successful in trading, and the US Department of Justice (DOJ) has announced an investigation into whether its success was due to illegally trading on insider information. More recently, Speculation Inc has had serious trading losses, causing its broker to declare a default on the margin loan. It also has fallen behind on its rent, and been sued by a former employee alleging she was fired due to due to gender bias.

What would be the effect of a Chapter 11 petition being filed by Speculation Inc on each of the (i) DOJ investigation, (ii) margin loan default; (iii) delinquent lease and (iv) employment discrimination lawsuit?

On the filling of the Chapter 11 petition, the worldwide automatic stay will come into effect.[[48]](#footnote-48) The automatic stay will be applied to the delinquent lease and the employment discrimination lawsuit. The other two hypotheses are not affected, because “[t]he stay is subject to certain statutory exceptions”.[[49]](#footnote-49) The DOJ investigation fits as "regulatory investigations"[[50]](#footnote-50) and the margin loan default is applied the exception "exercise of rights under commodity, forward, or security contract", because of the shares are held as collateral.

One effect on the secured creditor is that in the event of a 363 sale of the shares held as collateral, the creditor that hold the security interest “may “credit bid” by offsetting a portion of the purchase price of such property against the amount of its claim secured by the property”.[[51]](#footnote-51)

Considering that the lease of the office space is an executory contract, another effect would be that the debtor would have "[t]he ability to assume, reject or assume and assign"[[52]](#footnote-52) the contract.

Considering that the employee was fired, there is no employment contract in force, let alone a contract operating in collective bargaining agreements (CBAs), in which case the debtor could enter negotiation with an employee representative.[[53]](#footnote-53)

In a broad context of effects applied to creditors, the interested parties must be notified of the petition and the order to open the procedure.[[54]](#footnote-54)

Furthermore, HALL indicates that “[t]o demand payment on a claim, the creditor must file a proof of claim on or before the bar date specified by the court”.[[55]](#footnote-55) If the creditor secured by the shares does not prove his claim, this will not void his collateral.

Finally, if the plan is approved by the creditors and confirmed by the court, the creditors will have the effects of the reorganization foreseen in it.

**Question 4.2 [5 marks]**

Stella SA (Stella) is a an international cosmetics company incorporated in France, with its headquarters in Paris. Stella’s products are made in Italy and shipped to its retail stores in Europe (including England), Asia, and North America. Stella’s funding comes from a bank loan and Eurobonds, both of which are governed by English law. Stella’s retail sales have suffered due to pandemic-related closures and it is considering options to restructure its debt. One option is to use an English scheme of arrangement with respect to the Eurobonds. Could the English scheme of arrangement be recognized by a US bankruptcy court under Chapter 15, and would such recognition be as a foreign main or non-main proceeding?

According to HALL, “[t]he minimum requirement to be a debtor under any chapter of the Bankruptcy Code is the presence of the debtor or its place of business or any of its assets in the United States”.[[56]](#footnote-56) Since Stella's products ship to its retail stores in North America and assuming this includes the US, the minimum requirement to be a US debtor would be present.

A case under chapter 15 may be commenced in the district court of the US for the district (a) “in which the debtor has its principal place of business or principal assets in the United States”;[[57]](#footnote-57) (b) “if the debtor does not have a place of business or assets in the United States, in which there is pending against the debtor an action or proceeding in a Federal or State court”;[[58]](#footnote-58) or (c) “in a case other than those specified in paragraph (1) or (2), in which venue will be consistent with the interests of justice and the convenience of the parties, having regard to the relief sought by the foreign representative”.[[59]](#footnote-59)

Assuming that the English scheme of arrangement for which recognition is sought is a foreign main proceeding or foreign non main proceeding, that the petition for recognition was applied for the foreign representative, and the petition meets the requirements of § 1515 of the 11 USC.[[60]](#footnote-60) Then, the English scheme of arrangement could be recognized by a US bankruptcy court under Chapter 15.

To understand whether the English scheme of arrangement will be recognized as foreign main proceeding or a foreign non-main proceeding, it is necessary to know if it is pending in the country where the debtor has the center of its main interests (COMI) or an establishment.

A foreign main proceeding is defined as “a foreign proceeding pending in the country where the debtor has the center of its main interests”.[[61]](#footnote-61) HALL indicates that “[a] debtor’s COMI is presumed to be its place of incorporation, but this is rebuttable”.[[62]](#footnote-62) This presumption is set forth in § 1516(c) of 11 USC: "[i]n the absence of evidence to the contrary, the debtor’s registered office, or habitual residence in the case of an individual, is presumed to be the center of the debtor’s main interests".[[63]](#footnote-63)

Other factors should be used to determine the COMI according to HALL: (a) “location of headquarters”;[[64]](#footnote-64) (b) “location of management”;[[65]](#footnote-65) (c) “location of primary assets”;[[66]](#footnote-66) (d) “location of a majority of debtor’s creditors or a majority of the creditors that will be affected by the relief requested by the foreign representative”;[[67]](#footnote-67) and (e) “jurisdiction whose law will apply to most disputes”.[[68]](#footnote-68)

Considering the presumption, the COMI of Stella is in France, because is the country of incorporation. Its headquarters in Paris is another factor to consider, this could mean that the place of administration is also in France, although it is not possible to conclude in fact. It is also possible to consider that its retail stores in Europe include France.

The location of primary assets is in Italy, where the products are made and shipped around the word.

Considering that the operation is spread across several countries, it is not possible to establish concretely the location of a majority of debtor’s creditors and the jurisdiction whose law will apply to most disputes. However, Stella’s funding comes from a bank loan and Eurobonds, both of which are governed by English law, so it is possible to conclude that England would be the location of a majority of debtor’s creditors and the jurisdiction whose law will apply to most disputes.

HALL also indicates that “[a] debtor’s COMI should be ascertainable by its creditors or other third parties on the basis of objective evidence”.[[69]](#footnote-69) However, there are no elements that indicate what would be the COMI identifiable by creditors.

Therefore, both France, Italy and England have elements that justify determining that the country would be the COMI. In order to actually state that the COMI is in one of these countries, a more elaborate analysis of the specific case would be necessary.

On the other hand, the Bankruptcy Code provides that the foreign non-main procedure "means a foreign proceeding, other than a foreign main proceeding, pending in a country where the debtor has an establishment".[[70]](#footnote-70) In addition, the Bankruptcy Code defines establishment “means any place of operations where the debtor carries out a nontransitory economic activity”.[[71]](#footnote-71)

Considering Stella has retail stores in England, it is possible to say that Stella has an establishment in England. Therefore, the English scheme of arrangement can be recognized as a foreign non-main proceeding.

As explained above, it is not possible to conclude in which country Stella's COMI would be located. However, considering that the various factors involved make it possible to state that France could be the COMI and this is also the legal presumption, it seems that France would be the most appropriate COMI.

Thus, considering that there is an establishment in England, the English scheme of arrangement must be recognized in the USA as foreign non-main proceeding. Even so, it is worth noting that there are elements to state that England could be considered Stella's COMI.

**Question 4.3 [5 marks]**

ToyCo is an American toy company that has created a popular line of folding robot toys called Xblox. The toys are covered by several US patents. Currently, GameMart Inc (GameMart) has a 10-year exclusive license to manufacture Xblox and pays ToyCo monthly royalties. GameMart operates a factory in California that it leases from Land Corp on a longer term lease with seven years to go; the lease prohibits assignment without Land Corp’s consent. The Xblox toys are selling well, but GameMart’s other toy lines are doing poorly, so it is considering a Chapter 11 bankruptcy. Answer the following questions:

(i) Is the license to manufacture Xblox an executory contract?

According to HALL, “a contract is said to be executory if there are material unperformed obligations on both sides”.[[72]](#footnote-72) In the case, both sides have unperformed obligations, because ToyCo has the obligation to maintain the exclusive license, while GameMart has the obligation to pay monthly royalties. Therefore, the license to manufacture Xblox isa an executory contract.

(ii) Can GameMart transfer the Xblox license as part of 363 sale without ToyCo’s consent? Why or why not?

GameMart cannot transfer the Xblox license as part of 363 sale without ToyCo’s consent. The Bankruptcy Code states that an executory contract may not be assign, if the “applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to an entity other than the debtor or the debtor in possession, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties”.[[73]](#footnote-73) In the case, the intellectual property licensing law provides that the licensor cannot be compelled to accept performance from a transferee.[[74]](#footnote-74) In the specific context of asset sales, HALL states that "[l]icensees of patents and copyrights owned by the debtor are protected such that their licenses may not be terminated in connection with the sale of the intellectual property without their consent".[[75]](#footnote-75)

(iii) Can GameMart transfer the factory lease as part of 363 sale without Land Corp’s consent? Why or why not?

GameMart can transfer the factory lease as part of 363 sale without Land Corp’s consent. According to HALL, “the Bankruptcy Code abrogates contractual restrictions on assignment to enable the debtor to achieve a higher value for its assets than if such provisions were enforced”.[[76]](#footnote-76) The factory lease does not fall under any restriction of such rule. Therefore, the factory lease is assignable without consent, notwithstanding the landlord approval provision.

**\* End of Assessment \***

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19. 11 USC, § 1519(a)(1). [↑](#footnote-ref-19)
20. 11 USC, § 1519(a)(2). [↑](#footnote-ref-20)
21. 11 USC, § 1519(a)(3) and §1521(a)(3). [↑](#footnote-ref-21)
22. 11 USC, § 1519(a)(3) and §1521(a)(4). [↑](#footnote-ref-22)
23. 11 USC, § 1519(a)(3) and §1521(a)(7). [↑](#footnote-ref-23)
24. 11 USC, § 1502(4). [↑](#footnote-ref-24)
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